UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

JEFFERIES LLC, Plaintiff, v. WTW INVESTMENT COMPANY, LTD., PAULA TURNBULL KNOX, as trustee of Turnbull Marital Trust, WILLIAM STANTON, JANET STANTON, JEFFREY DWORKIN, ROBERT ANDERSON, ALEJANDRO CABRERA, JOHN GONZALEZ, KENNETH BARNETT, MARK A. HADJA, BROOKS BARKLEY, SARAH BARKLEY, ANDREW WILLIAMS, RICHARD HOEDEBECK, SALLY HOEDEBECK, BETH ERWIN, BRIAN BECK, STEVEN RIEBEL, as trustee of Riebel Living Trust, JENNIE D. PRICE, RENOUARD INVESTMENTS, LLC, PAUL THOMPSON, DAVID N. PEDERSON, TODD R. BROWN, JEFFREY MILLER, MICHAEL SULLIVAN, LORI BOWEN, PHYLLIS K. CLARK, RICHARD LONGORIA, MARK E. TRIVETTE, TARAK PATEL, MAROON FEGHALI, JOSEPH N. FEGHALI, ELIE N. FEGHALI, ROBERT S. TYLER, DONNELLA R. TYLER, THOMAS G. KEYSER, CONSTANCE LINDSEY, and RUSTY McDOWELL, Defendants.	CIVIL ACTION No. 3:17-CV-0332-D

JEFFERIES LLC'S RESPONSE AND BRIEF IN OPPOSITION TO DEFENDANTS' MOTION FOR SUMMARY JUDGMENT AND IN SUPPORT OF ITS CROSS-MOTION FOR SUMMARY JUDGMENT

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Plaintiff Jefferies LLC ("Jefferies") respectfully submits this brief in opposition to the motion for summary judgment filed by Defendants and in support of its cross-motion for summary judgment.

I. PRELIMINARY STATEMENT

Defendants in this action are a group of aggrieved investors who improperly commenced arbitration against Jefferies under the auspices of the Financial Industry Regulatory Authority ("FINRA"), asserting claims for losses they suffered arising out of their purchase of preferred stock in Palmaz Scientific, Inc. ("Palmaz"), a now-defunct biotechnology company. But Rule 12200 of the FINRA Code of Arbitration Procedure for Customer Disputes (the "FINRA Code") provides that certain disputes may be resolved by means of arbitration ***only*** between member firms and their "customer[s]," and Defendants concede that they have ***never*** been customers of Jefferies. Accordingly, the Court should issue a declaration that Jefferies is not required to arbitrate Defendants' claims, as well as an injunction restraining Defendants from pursuing claims against it in the Arbitration, on the grounds that Defendants are not and were never customers of Jefferies under FINRA Rule 12200.

Notably, Defendants do not dispute any of the factual allegations in Jefferies' Complaint. (*See* Defendants' Original Answer and Motion for Summary Judgment, dated February 17, 2017 ("Ans.") (Appendix ("App.") at 1–14) ¶ 5.) Critically, Defendants concede the following facts which are dispositive of this issue:

- They have *never* held any customer accounts with Jefferies (*id.* ¶ 6);
- They did not purchase their Palmaz shares from Jefferies, but remarkably did so through another FINRA member, WFG Investments, Inc. ("WFG"), or from the issuer directly (*id.* ¶ 7); and
- They have never entered into any arbitration agreement with Jefferies (*id.* ¶ 8).

Indeed, Defendants have not identified ***any*** direct relationship between them and Jefferies, because there is none. Faced with these fatal facts, Defendants offer the implausible and logically flawed argument that because they are not brokers or dealers—two categories expressly excluded from the definition of "customer" under the FINRA Code—they are "customers in general" entitled to arbitrate their claims against Jefferies. (*See* Ans. ¶¶ 35, 41–43.) However, that same argument has already been tried and squarely rejected by multiple courts. *See, e.g., Fleet Bos. Robertson Stephens, Inc. v. Innovex, Inc.*, 264 F.3d 770, 772 (8th Cir. 2001) (rejecting argument that FINRA Rule 12200 defines "customer" by "negative inference" to mean "everyone who is not a broker or dealer").

The sole issue before the Court is a pure question of law (*see* Ans. ¶ 11): whether Defendants—who have never held accounts with Jefferies, did not purchase their Palmaz shares from Jefferies, and have never entered into any written arbitration agreement with Jefferies—are "customer[s]" of Jefferies within the meaning of FINRA Rule 12200. On the authority of the Second, Fourth, Eighth, and Ninth U.S. Courts of Appeal, the answer is an unequivocal no. Jefferies is not bound to participate in the Arbitration with Defendants, whose only possible recourse would be to bring their claims before a court of competent jurisdiction. An alternative holding would lead to the irrational outcome that, by virtue of its membership in FINRA, Jefferies could be compelled to arbitrate *any* dispute with *any* claimant who ever transacted with *any other* FINRA member, no matter how tenuous the connection to Jefferies. Such an illogical outcome has been rejected by numerous courts.

In view of the *undisputed* facts of this case, and because Defendants have no legitimate legal basis to compel Jefferies to arbitrate, Jefferies respectfully requests that the Court deny Defendants' motion for summary judgment, grant Jefferies' cross-motion for summary judgment, and issue an order (i) declaring that Jefferies is not obligated to arbitrate this dispute with Defendants and (ii) permanently enjoining Defendants from proceeding with the Arbitration against Jefferies.

II. STATEMENT OF UNDISPUTED FACTS[1]

Jefferies is a licensed broker-dealer and a member firm of FINRA. (Compl. ¶ 5; Ans. ¶ 5.) Defendants named Jefferies as a respondent in the Arbitration, which they commenced by filing a Statement of Claim with FINRA on or about December 20, 2016. (Compl. ¶ 50; Ans. ¶ 1.) Defendants also named WFG, another FINRA member, as a respondent in the Arbitration. (Compl. ¶ 50; Ans. ¶ 9.) The claims asserted in the Arbitration concern losses that Defendants allegedly incurred in connection with their purchase of preferred shares of Palmaz. Defendants claim that they relied on private placement memoranda ("PPMs") originally prepared by Jefferies but provided to them independently by WFG. (Compl. ¶ 52; Ans. ¶ 9.)

Defendants do not dispute any of Jefferies' factual allegations. Indeed, in their Answer to the Complaint, they expressly state that: "Defendants do not dispute Plaintiff's factual allegations." (Ans. ¶ 5.) Notably, Defendants acknowledge that they never held any accounts with Jefferies. (*Id.* ¶ 6.) Defendants also concede that they did not purchase the Palmaz preferred shares from Jefferies, but either through WFG or directly from the issuer. (Ans. ¶ 7; Compl. ¶ 67.) Defendants do not dispute the absence of any agreement to arbitrate between the parties, conceding expressly that "[n]o such agreement exists." (Ans. ¶ 8; Compl. ¶ 54.) Since Defendants concede all of the facts alleged in Jefferies' Complaint, the sole remaining controversy between the parties is whether Defendants are "customers" of Jefferies under FINRA Rule 12200 and thus may compel Jefferies to arbitrate their claims before FINRA. (*See, e.g.*, Ans. ¶ 11 ("Defendants ***only*** dispute Plaintiff's ***legal conclusion***

[1] Jefferies alleged the essential facts of this dispute in its Original Complaint, dated February 3, 2017 ("Compl." (App. at 15–25)), and those facts are undisputed. (*See* Ans. ¶ 5.) On March 6, 2017, Jefferies filed an Amended Complaint (App. at 26 –36) containing the same undisputed factual allegations to remedy certain technical defects in its Original Complaint's jurisdictional claims, in accordance with the Court's order of February 13, 2017.

which asserts Defendants were not 'Customers' as defined by Rule 12200 of the FINRA Code of Arbitration. This allegation is the central issue in this declaratory judgment action and calls for application of the law to the undisputed facts.") (emphasis added).) Therefore, this dispute is ripe to be resolved on summary judgment, and Jefferies is entitled to summary judgment as a matter of law.

III. LEGAL STANDARDS

1. Summary Judgment

Summary judgment is appropriate if no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(a). To be entitled to summary judgment on a claim or defense for which it will have the burden of proof, a party "must establish 'beyond peradventure all of the essential elements of the claim or defense.'" *Bank One, Tex., N.A. v. Prudential Ins. Co. of Am.*, 878 F. Supp. 943, 962 (N.D. Tex. 1995) (Fitzwater, J.) (quoting *Fontenot v. Upjohn Co.*, 780 F.2d 1190, 1194 (5th Cir. 1986)). This means that the moving party must demonstrate the absence of genuine and material fact disputes and that it is entitled to summary judgment as a matter of law. *See Martin v. Alamo Cmty. Coll. Dist.*, 353 F.3d 409, 412 (5th Cir. 2003). Where, as here, the parties cross-move for summary judgment, the court must review "each motion independently, viewing the evidence and inferences in the light most favorable to the nonmoving party." *Mid–Continent Cas. Co. v. Bay Rock Operating Co.*, 614 F.3d 105, 110 (5th Cir. 2010) (quoting *Ford Motor Co. v. Tex. Dep't of Transp.*, 264 F.3d 493, 498 (5th Cir. 20010)) (alteration and quotation marks omitted).

2. Declaratory and Injunctive Relief

Under the Declaratory Judgment Act, 28 U.S.C. § 2201(a), "[i]n a case of actual controversy within its jurisdiction . . . any court of the United States . . . may declare the rights and other legal relations of any interested party seeking such declaration[.]" The requirement of an "actual controversy" derives from the prohibition against federal courts issuing advisory opinions. *See Golden v. Zwickler*, 394 U.S. 103, 108 (1969). "[T]he question in each case is whether the facts alleged, under all the circumstances, show that there is a substantial controversy, between parties having adverse legal interests of sufficient immediacy and reality to warrant the issuance of a declaratory judgment." *Vantage Trailers, Inc. v. Beall Corp.*, 567 F.3d 745, 748 (5th Cir. 2009) (quoting *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 127 (2007)).

To demonstrate entitlement to permanent injunctive relief, the movant must establish that: "(1) it has achieved actual success on the merits; (2) it has sustained irreparable injury or there is no adequate remedy at law; (3) considering the balance of the hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) the injunction will not disserve the public interest." *Atlas Trading Conglomerate Inc. v. AT&T Inc.*, No. 3:15-CV-0404-K, 2016 WL 5870857, at *7 (N.D. Tex. Oct. 5, 2016) (citing *ITT Educ. Servs., Inc. v. Arce*, 533 F.3d 342, 347 (5th Cir. 2008)).

III. ARGUMENTS AND AUTHORITIES

1. Jefferies is Entitled to Summary Judgment Because, As a Matter of Law, Defendants Cannot Compel Jefferies to Arbitrate Their Claims.

Defendants concede in their motion for summary judgment that the sole remaining controversy between the parties is whether Defendants are "customers" of Jefferies under FINRA Rule 12200 and thus may compel Jefferies to arbitrate their claims before FINRA. This question invites the Court's "application of the law to the undisputed facts." (Ans. ¶ 11.) The application of law to the undisputed facts in this case makes abundantly clear that Jefferies is entitled to summary judgment as a matter of law, and Defendants are not.

"[T]he first task of a court asked to compel arbitration of a dispute is to determine whether the parties agreed to arbitrate that dispute." *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985). Defendants cannot compel Jefferies to arbitrate on the basis of any written arbitration agreement because, as they expressly admit, "[n]o such agreement exists." (Ans. ¶ 8.) Trying to get around this admission, Defendants purposefully misconstrue the requirements set forth in FINRA Rule 12200, which provides that:

> Parties must arbitrate a dispute under the [FINRA] Code if:
>
> • Arbitration under the [FINRA] Code is either:
> (1) Required by a written agreement, or
> (2) Requested by the customer;
>
> • The dispute is between a customer and a member or associated person of a member; and
>
> • The dispute arises in connection with the business activities of the member . . . .

The plain language of Rule 12200 states that Defendants may initiate a FINRA arbitration against Jefferies *only* if they are or were "customer[s]" of Jefferies. Jefferies is entitled to summary judgment as a matter of law because, as detailed below, Defendants' purported "customer" status is belied by the undisputed facts and is premised on an implausible reading of the FINRA Code that has been squarely rejected by multiple federal circuit courts.

As discussed further below, the only case relied upon by Defendants in their brief, *Bensadoun v. Jobe-Riat*, 316 F.3d 171 (2d Cir. 2003), is inapposite and distinguishable. It has also been *superseded* by a later decision of the same court which sets forth a bright line definition for the term "customer" under the FINRA Code, which Defendants do not meet. *See Citigroup Global Markets Inc. v. Abbar,* 761 F.3d 268, 275 (2d Cir. 2014) ("We hold that a 'customer' under FINRA Rule 12200 is one who, while not a broker or dealer, either (1) ***purchases a good or service*** from a FINRA member, or (2) ***has an account*** with a FINRA member.") (emphasis added). Under the plain reading of the FINRA Code and clear judicial precedent, at no point in time have Defendants ever been "customer[s]" of Jefferies, a fact which Defendants themselves have now conceded. As such, they cannot invoke Rule

12200 to compel FINRA arbitration of their claims against Jefferies and thus wholly fail to establish that they are entitled to judgment as a matter of law.

A. Defendants Cannot Compel Jefferies to Arbitrate Unless They Establish a Customer Relationship With Jefferies, Which They Admit Does Not Exist.

Defendants misconstrue the FINRA Code and established legal precedent and argue that they do not need to establish customer relationships with Jefferies, because they are "customers in general." (*See* Ans. ¶ 35.) Incredibly, Defendants do not even identify whose customers they are. If such allegations were sufficient to satisfy FINRA Rule 12200, it would lead to the irrational result that "any customer of a FINRA member [could] compel arbitration against *any other* FINRA member, regardless of whether there had been any relationship or contact between the parties." *Waterford Inv. Servs., Inc. v. Bosco*, No. 3:10CV548-REP, 2011 WL 3820723, at *6 (E.D. Va. July 29, 2011) (emphasis in original), *report and recommendation adopted*, No. 3:10CV548, 2011 WL 3820496 (E.D. Va. Aug. 26, 2011), *aff'd*, 682 F.3d 348 (4th Cir. 2012). Unsurprisingly, Defendants have not identified any authority to support this illogical argument, because none exists.

To the contrary, in order to compel Jefferies to a FINRA arbitration, Defendants must show that they were customers *of Jefferies*. That is because, "[w]hen it accepted FINRA Rule 12200, [Jefferies] agreed to arbitrate disputes with its customers, *not with those who fall outside that category*." *Raymond James Fin. Servs., Inc. v. Cary*, 709 F.3d 382, 386 (4th Cir. 2013) (emphasis added); *see also AXA Distributors, LLC v. Bullard*, No. 1:08-CV-188-WKW, 2008 WL 5411940, at *3 (M.D. Ala. Dec. 24, 2008) ("Because there is no independent written arbitration agreement between Plaintiff and Defendants, the dispute will be arbitrated only if Defendants were 'customers' of AXA Distributors, thereby invoking the FINRA Rules."). However, Defendants have already conceded that they are not, and have never been customers of Jefferies. (*See* Compl. ¶ 56; Ans. ¶ 5.) That admission alone forecloses FINRA arbitration of their claims against Jefferies under Rule 12200.

B. Jefferies Has Not Provided Any Investment or Brokerage Services to Defendants.

Defendants concede that they *never* held accounts with Jefferies. (Ans. ¶ 6.) They admit that they purchased their Palmaz preferred shares, *not through Jefferies*, but either through WFG or from the issuer directly. (*Id.* ¶ 7.) They likewise do not dispute that Jefferies *never* entered into any written agreement with any of the Defendants. (*Id.* ¶ 5; Compl. ¶ 54.) Instead, Defendants point to a single, extremely attenuated connection to Jefferies: that they purportedly relied on a PPM allegedly prepared by Jefferies prior to their Palmaz investments and independently provided to them by WFG. (*See* Ans. ¶¶ 1, 9.)

However, the case law is clear that "the mere circulation of a private placement memorandum . . . does not establish a customer relationship . . . sufficient to invoke FINRA arbitration." *Berthel Fisher & Co. Fin. Servs. v. Larmon*, No. CIV. 11-889 ADM/JSM, 2011 WL 3294682, at *7 (D. Minn. Aug. 1, 2011), *aff'd*, 695 F.3d 749 (8th Cir. 2012). Even if Jefferies had drafted the PPM that was later relied upon by the Defendants, Defendants still could not compel Jefferies to arbitration on that basis alone, because, in determining whether a dispute is subject to arbitration before FINRA, "the provision of investment or brokerage related services is only half of the picture." *Berthel Fisher & Co. Fin. Servs., Inc. v. Larmon*, 695 F.3d 749, 753 (8th Cir. 2012) (internal quotation marks omitted). "[N]ot only must the FINRA member firm provide those services, but it also must provide those services *to the customer* either directly or through its associated persons." *Id.* (emphasis in original). Since Jefferies did not provide any investment or brokerage related services directly to any of the Defendants, and did not provide the PPM to any of the Defendants, it does not have a customer relationship with any of them. Therefore, Defendants cannot compel Jefferies to arbitration and the Court should grant Jefferies' cross-motion for summary judgment.

C. Defendants Fall Short of Every Other Court of Appeals Definition of "Customer" Under the FINRA Code.

The Second, Fourth, Eighth and Ninth Circuits have all set forth definitions of the term "customer" for the purposes of FINRA Rule 12200, and each of the Court of Appeals decisions would bar Defendants from compelling Jefferies to a FINRA arbitration on this set of undisputed facts.

In *Citigroup Global Markets Inc. v. Abbar*, 761 F.3d 268 (2d Cir. 2014), the Second Circuit set forth a bright-line definition of a "customer" for the purpose of FINRA Rule 12200: "We hold that a 'customer' under FINRA Rule 12200 is one who, while not a broker or dealer, either (1) purchases a good or service from a FINRA member, or (2) has an account with a FINRA member." *Id*. at 275. Defendants utterly fail to meet the *Abbar* test: they admit that they did not purchase any goods or services from Jefferies and that they never held any accounts with Jefferies.

The Fourth Circuit, in *UBS Financial Services, Inc. v. Carilion Clinic*, 706 F.3d 319 (4th Cir. 2013), held that "'customer,' as that term is used in the FINRA Rules, refers to one, not a broker or a dealer, who purchases commodities or services from a FINRA member in the course of the member's business activities insofar as those activities are regulated by FINRA—namely investment banking and securities business activities." *Id*. at 327. Defendants again fail to meet the Fourth Circuit's definition because they admit that they have not purchased any financial products or services from Jefferies.

In construing the analogous provision in the code governing arbitration under the National Association of Securities Dealers ("NASD"), FINRA's predecessor, the Eighth Circuit narrowly defined "customer" to "refer[] to one involved in a business relationship with [a FINRA] member that is related directly to investment or brokerage services." *Fleet Bos.*, 264 F.3d at 772. In light of the undisputed facts of this case, it is clear that Defendants never shared a "business relationship" with Jefferies, a fact which Defendants concede.

The Ninth Circuit, relying on precedent from the Second and Fourth Circuits, held that a "customer" is "a non-broker and non-dealer who purchases commodities or services from a FINRA member in the course of the member's FINRA-regulated business activities, *i.e*., the member's investment banking and securities business activities." *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 741 (9th Cir. 2014). The Ninth Circuit's definition also undermines Defendants' position because—it bears repeating—Defendants admit that they did not purchase any commodities or services from Jefferies, including the Palmaz securities at issue in the Arbitration.

At least two District Court decisions from the Fifth Circuit have construed the meaning of "customer" under FINRA Rule 12200. In *Credit Suisse Sec. (USA) LLC v. Sims*, No. H–13–1260, 2013 WL 5530827 (S.D. Tex. Oct. 4, 2013), the District Court enjoined an individual from compelling a FINRA arbitration because she had no contract or relationship with the two FINRA member firms that were named in the arbitration. *Id*. at *3. The defendant-claimant in *Sims* purchased a security on the secondary market through a third party broker-dealer, but like in this case, had improperly commenced a FINRA arbitration against two financial services firms with whom she had no prior dealings. *Id*. Another District Court in this Circuit held that the term "customer" under the FINRA Code "appears to require a direct relationship, contractual or otherwise." *Pershing LLC v. Bevis*, No. 13–672–JJB–RLB, 2014 WL 1818098, at *2 (M.D. La. May 7, 2014), *aff'd*, 606 F. App'x 754 (5th Cir. 2015). In that case, the court enjoined a pending FINRA arbitration because of the lack of a "direct customer relationship" as required by Rule 12200. *Id*. at *2–3. Defendants have admitted that they do not have any, let alone a *direct*, customer relationship with Jefferies. (*See* Compl. ¶¶ 55–57; Ans. ¶ 5.)

Conspicuously absent from Defendants' motion for summary judgment is any mention of the above-described precedent, which itself reveals the fatal flaws in Defendants' erroneous attempt to compel Jefferies to arbitration. The weight of authority is clear: since Defendants are not and were never "customer[s]" of Jefferies under *any* plausible definition, they cannot invoke Rule 12200 to compel FINRA arbitration of their dispute with Jefferies. As such, this Court should deny Defendants' motion for summary judgment and grant Jefferies' cross-motion for summary judgment.

D. Defendants' Reliance on *Bensadoun* is Misplaced and Ignores Subsequent Second Circuit Authority.

In a desperate bid to ignore all relevant case law and precedent on this issue, Defendants rely upon a single Second Circuit case, which is not only outdated, but also entirely inapposite. (*See* Ans. ¶¶ 29 –32, 34–36, 38–39, 42 (citing *Bensadoun*).) In light of Defendants' exclusive and extensive reliance on *Bensadoun*, a detailed discussion of that decision is warranted.

Bensadoun involved an arbitration brought by a group of investors against multiple respondents, including Bensadoun, a stockbroker. *Bensadoun*, 316 F.3d at 173. The arbitration was brought under the NASD Code, which, mirroring FINRA Rule 12200, provided that "[a]ny dispute, claim, or controversy . . . between a customer and a member and/or associated person arising in connection with the business of such member or in connection with the activities of such associated persons shall be arbitrated under this Code." NASD Code of Arbitration Procedure Rule 10301(a).

The claimants alleged that Bensadoun orchestrated a scheme to defraud them with an "unnamed co-conspirator/respondent" by the name of Autard. *Bensadoun*, 316 F.3d at 173. It was undisputed that the claimants were "customers" of Autard, and that Bensadoun was an "associated person" under the NASD Rules. *Id*. at 176. Bensadoun brought an action in the Southern District of New York for declaratory and injunctive relief, contending that the investors had no right to arbitrate their claims against him. *Id*. at 174. The issue before the Second Circuit was "whether there needs to be a direct customer relationship between the associated person [Bensadoun] and the purported customer [the claimants]." *Id*. at 176. The Second Circuit remanded to the district court to resolve a "factual issue": whether, as the investors alleged, "Bensadoun was complicit in a fraudulent scheme that involved misleading the Investors into believing that they were customers of his." *Id*. at 177. The case is thus inapposite. Here, Defendants have never alleged any dealings with Jefferies, either directly or through an "associated person."

Moreover, the legal principles that Defendants try to claim that *Bensadoun* stands for are neither accurate nor helpful to their case. *First*, Defendants quote the *Bensadoun* court's purported instruction that "any ambiguity in the meaning of 'customer' . . . should be construed in favor of arbitration." (Ans. ¶ 30.) However, the Second Circuit expressly acknowledged that it was paraphrasing "dicta" from a previous case, which it then went on to distinguish and declined to follow. *Bensadoun*, 316 F.3d at 176 (citing *John Hancock Life Ins. Co. v. Wilson*, 254 F.3d 48, 59 (2d Cir. 2001)). And, as discussed further below, "this argument has been rejected more than once" by subsequent Second Circuit cases. *See Abbar*, 761 F.3d 268, 274 (2d Cir. 2014). *Second*, the Second Circuit *did not* address the issue of whether "arbitration is mandatory when the claimants are only customers in general, and not customers 'of' the respondent" which is the only issue in this case. (Ans. ¶ 35.) Rather, the question in *Bensadoun* was whether the investor claimants were "customers" of an "associated person" despite the involvement of an unassociated intermediary in the impugned transactions. *Bensadoun,* 316 F.3d at 177–78. Here, by contrast, it is undisputed that Defendants had no dealings with Jefferies, either directly or through associated persons, a fact which Defendants themselves admit.

Furthermore, contrary to Defendants' misrepresentation, *Bensadoun* is not "authoritative" on the construction of Rule 12200—either for this Court or even in the Second Circuit itself. The leading Second Circuit authority on FINRA Rule 12200 is *Citigroup*

Global Markets Inc. v. Abbar, a case decided *eleven years* after *Bensadoun*. As discussed in Section 1(c), in *Abbar*, the Second Circuit undertook a detailed examination of the prior relevant cases, including *Bensadoun*, and set forth a bright-line definition of "customer" within the meaning of FINRA Rule 12200: "one who, while not a broker or dealer, either (1) ***purchases a good or service*** from a FINRA member, or (2) ***has an account*** with a FINRA member." 761 F.3d at 275 (emphasis added). As discussed above, Defendants satisfy neither requirement.

E. The Fact That Defendants Are Not Brokers or Dealers Does Not Render Them Customers of Jefferies.

FINRA Rule 12100(i) provides in full that: "A customer shall not include a broker or dealer." Citing this rule, Defendants mistakenly assert that "[a] customer is defined *through exclusion* as *anyone* other than a broker dealer [*sic*]." (Ans. ¶ 43 (emphasis added).) But courts have clearly held that "Rule 12100(i) does not provide a comprehensive definition" of the term "customer" under the FINRA Rules, "but simply *limits* the scope of the term[.]" *Morgan Keegan & Co. v. Silverman*, 706 F.3d 562, 566 (4th Cir. 2013) (emphasis added). Another district court expressly rejected Defendants' misreading of this Rule, and held that:

> [Rule 12100(i)] does not define "customer," rather it states that "A customer shall not include a broker or dealer." [Defendant's] argument fails to acknowledge that the word "customer" has an accepted meaning . . . **Rule 12100(i) does not provide the meaning of the word "customer,"** rather it uses a word with an accepted meaning, and then articulates two classes of persons or entities who should be excluded from being considered a customer. This exclusion serves the purpose of segregating customer claims from other claims which should be brought under the FINRA Industry Code. Where FINRA's Customer Code applies to customer disputes, the Industry Code governs arbitration of disputes between or among "members" and "associated persons," most of whom are brokers, dealers, or registered representatives.

Morgan Keegan & Co. Inc. v. Johnson, No. 2:11CV502, 2011 WL 7789796, at *5 (E.D. Va. Dec. 22, 2011) (emphasis added).

Indeed, many other courts across the country have clearly rejected Defendants' untenable argument that, merely because they are neither brokers nor dealers, they are automatically "customer[s]" within the meaning of Rule 12200. *See, e.g.*, *Fleet Bos. Robertson Stephens, Inc. v. Innovex, Inc.*, 264 F.3d 770, 772 (8th Cir. 2001) ("AdFlex argues that by negative inference this definition means a 'customer' is everyone who is not a broker or dealer. We agree with the district court that this definition is too broad."); *see also SunTrust Banks, Inc. v. Turnberry Capital Mgmt. LP*, 945 F. Supp. 2d 415, 421 (S.D.N.Y. 2013) ("[C]ourts have held that the term 'customer' must have a more limited meaning than simply 'all entities other than brokers or dealers'"). "Defendants' interpretation of the definition of 'customer' would imply that a party seeking to compel arbitration pursuant to the FINRA rules need not have an actual customer relationship with any FINRA member; rather, the party need only not be a broker or dealer. Such an interpretation . . . would be absurd." *UBS Secs. LLC v. Voegeli*, 684 F. Supp. 2d 351, 356 (S.D.N.Y. 2010). Notably, Defendants make no attempt to explain why this case presents an exception to the widely-accepted precedent concerning the plain meaning of FINRA Rule 12200.

F. The Interests of Public Policy Weigh Against Compelling Arbitration Against a Non-Consenting Party Like Jefferies.

Although the federal policy in favor of arbitration is a matter of black letter law, it has no application where, as here, the dispute is whether the parties even agreed to arbitrate at all. *See, e.g.*, *Hyundai Merch. Marine Co. v. Conglobal Indus., LLC*, No. 3:15-CV-3576-G, 2016 WL 695649, at *2 (N.D. Tex. Feb. 22, 2016) ("While there is a strong federal policy favoring arbitration, the court does not yield to this policy when making the initial threshold determination about the existence of an agreement to arbitrate."). Private arbitration is a matter of contract. Thus, "where a party contends that it has not signed any agreement to arbitrate, the court must first determine if there is an agreement to arbitrate before any additional dispute can be sent to arbitration." *Will–Drill Res., Inc. v. Samson Res. Co.*, 352

F.3d 211, 218 (5th Cir. 2003). Defendants cannot simply recite the federal pro-arbitration policy in order to bypass the requirement of a "validly formed and enforceable arbitration agreement" as a condition to compel arbitration. *See Granite Rock Co. v. Int'l Bhd. of Teamsters*, 561 U.S. 287, 301 (2010); *see also Raymond James Fin. Servs., Inc. v. Cary*, 709 F.3d 382, 385 (4th Cir. 2013) (a non-customer seeking to compel a FINRA arbitration "overlook[ed] the fact that a court cannot apply any presumption in favor of arbitration unless there already exists an enforceable arbitration agreement between the parties").

Indeed, compelling arbitration in the absence of a valid agreement would "discourage entities from agreeing to arbitrate at all out of fear that such agreements would be stretched too far in the course of judicial construction. This in itself would undermine the federal policy favoring arbitration." *Sims*, No. H–13–1260, 2013 WL 5530827, at * 4 (quoting *Raymond James Fin. Servs., Inc. v. Cary*, 709 F.3d 382, 388 (4th Cir. 2013)). This concern is particularly resonant in the present case, because "ensuring that FINRA members will not be subjected to terms that could not have been reasonably envisioned when joining FINRA serves the purpose of encouraging participation in organizations that have arbitration rules, such as FINRA, and is consistent with the federal policy favoring resolution in arbitration *when the parties have contractually agreed to it.*" *Virchow Krause Capital, LLC v. North*, No. 11 C 8169, 2012 WL 1952731, at *4 (N.D. Ill. May 30, 2012) (emphasis added). Jefferies could never have envisioned when it joined FINRA that it would be compelled to arbitrate an alleged dispute with non-customers with whom it never had any direct dealings. To compel Jefferies to arbitrate with Defendants in these circumstances would *undermine* the federal policy favoring arbitration.

2. The Court Should Issue a Permanent Injunction Restraining Defendants from Continuing the Arbitration Against Jefferies.

As set forth above, to demonstrate entitlement to permanent injunctive relief, the movant must establish that: (1) it has achieved actual success on the merits; (2) it has sustained irreparable injury or there is no adequate remedy at law; (3) considering the balance of the hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) the injunction will not disserve the public interest. *Atlas Trading Conglomerate Inc. v. AT&T Inc.*, No. 3:15-CV-0404-K, 2016 WL 5870857, at *7 (N.D. Tex. Oct. 5, 2016) (citing *ITT Educ. Servs., Inc. v. Arce,* 533 F.3d 342, 347 (5th Cir. 2008)).

For all of the reasons discussed in Section 1, the undisputed facts establish that Jefferies cannot be compelled to arbitrate Defendants' claims, and therefore, Jefferies prevails on the actual merits of its claim for permanent injunctive relief. Moreover, Jefferies has and will continue to "suffer irreparable harm if Defendants are not enjoined from proceeding in the FINRA arbitration," because, otherwise, Jefferies would be forced to expend further "time and resources arbitrating a dispute that is not arbitrable." *Deutsche Bank Sec. Inc. v. Roskos*, No. 15CV534-LTS, 2016 U.S. Dist. LEXIS 102682, at *17 (S.D.N.Y. Aug. 04, 2016). The issuance of this equitable remedy in favor of Jefferies is warranted because the irreparable harm it has and will continue to suffer in connection with the Arbitration far outweighs the hardship of depriving Defendants of the "futile exercise" of arbitrating non-arbitrable claims. *Morgan Keegan & Co. v. McPoland*, 829 F. Supp. 2d 1031, 1036 (W.D. Wash. 2011). Finally, the permanent injunction sought by Jefferies would not disserve the public interest. On the contrary, "[w]here a party has not agreed to submit a dispute to arbitration, *the public has an interest in ensuring that the arbitration does not proceed*." *Sims*, 2013 WL 5530827, at *4 (emphasis added).

IV. CONCLUSION

For the reasons set forth above, Jefferies respectfully requests that this Court: (1) deny Defendants' motion for summary judgment; (2) grant Jefferies' motion for summary judgment; (3) issue orders declaring that Jefferies is not required to arbitrate the claims asserted by Defendants in the Arbitration, and permanently enjoining Defendants from pursuing the Arbitration against Jefferies; and (4) grant Jefferies such other and further relief as the Court considers just and proper.

Dated: March 10, 2017

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned certifies that on March 10, 2017, a true and correct copy of the foregoing document and related attachments have been served on Plaintiff's counsel via electronic mail.

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